DEVELOPMENTS IN REVIEW OF ARBITRATION AWARDS FOR ERROR OF LAW

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More than 15 years ago in Moncharsh v. Heily & Blasé, 3 Cal. 4th 1 (1992), the California Supreme Court purported to resolve a conflict among lower courts over whether an arbitration award was subject to review for error of law.

In considering an appeal by a law firm associate from an arbitration decision upholding a provision in his employment agreement apportioning fees paid by clients who retained him upon his resignation, the Court ruled that, with limited exceptions, an arbitrator's award was not reviewable for error of fact or law. Instead, the grounds of review were limited to those specified in Code of Civil Procedure Section 1286.2.

Two exceptions were recognized by the Moncharsh court. One is the situation in which an unlicensed individual attempts to recover compensation for services for which a license is required. Allowing recovery in such a case would be contrary to the strong California public policy reflected in the licensing statute. Moncharsh, 3 Cal. 4th at 31; see, e.g., Loving & Evans v. Blick, 33 Cal. 2d 603 (1949)(construction contractor).

The other is when "granting finality to an arbitrator's decision would be inconsistent with the protection of a party's statutory rights." Moncharsh. 3 Cal. 4th at 32. The Moncharsh court cited Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 225-27 (1987), for this proposition. However, it was enunciated by the Supreme Court initially in Mitsubishi Motors Corp. v. Soler-Chrysler Plymouth, Inc., 473 U.S. 614 (1982), in which the Court enforced an agreement to arbitrate a Sherman Act claim in Japan, but assured the losing litigant that it would take a look at the outcome to see how the Japanese arbitrators coped with American antitrust law.

Just last year, however, in the case of Cable Connection, Inc. v. DirecTV, Inc., 44 Cal. 4th 1334 (2008), the Court added a third, potentially huge exception.

To understand this exception, it is necessary to have in mind that one of the grounds of review of an arbitration award specified in CCP Section 1286.2 is that "the arbitrators exceeded their powers." Code of Civil Procedure Section 1286.2(a)(4).

In the wake of Moncharsh, many dispute resolution clause drafters speculated about what the Court would do if an arbitration clause limited the power of the arbitrator to deciding a case in accordance with applicable substantive law.

As it turned out according to the Cable Connection 5-2 majority, limiting the power of an arbitrator to deciding the law correctly lays an effective foundation to obtain review for error of law, provided the arbitration clause imposes the limit "explicitly and unambiguously." In Cable Connection, the clause provided that "the arbitrators shall not have the power to commit errors of law or legal reasoning, and the award may be vacated" if they do.

By way of contrast, only a few weeks earlier, the Court in Gueyffier v. Ann Summers, Ltd., 43 Cal. 4th 1179 (2008), had upheld an arbitral award against a contention the arbitrator had exceeded his power. The arbitration clause in the Gueyffier case provided that "in no event may the material provisions of this Agreement be modified or changed by the arbitrator." The arbitrator premised his award in part on finding reason to excuse performance of a notice of default and opportunity to cure clause. The Court noted that the power limitation was "explicit," but did not "unambiguously" prohibit the arbitrator from excusing performance.

Given the opportunity created by Cable Connection, the questions become whether arbitration clause drafters should avail themselves of the option of providing for review of legal error and whether such a clause would prove to be effective.

Whereas it formerly was likely that arbitration awards once rendered would be accepted and performed, the submission of larger and more

important disputes to arbitration has led to an increasing desire for a "second look" at arbitral decisions.

There can be little doubt that an effort to obtain review of an award in the courthouse holds the potential for increasing both the time and expense involved in resolving a dispute in arbitration. Taken together with increased discovery effort, the tendency is to make arbitration more and more like litigation.

Clause drafters must ask whether other benefits of arbitration, such as privacy and the ability to have a voice in and veto over the decision maker, continue to make it a desirable alternative to litigation, even though it may no longer be quicker and more economical.

In addition, would the time and money that might be spent in curing error on review be better spent in forestalling error by more assiduous attention to arbitrator selection?

Apart from whether it will be desirable to limit the power of an arbitrator to deciding legal issues correctly, clause drafters need also consider whether such a limitation will be as effective as might be supposed on first reading of Cable Connection.

Suppose the contract in which an arbitration clause is to be included involves an out-of-state party. Suppose the law of the sister state does not allow parties to provide indirectly for review of legal error, as authorized by Cable Connection. Can a choice of law clause be drafted to save a limitation on the power of arbitrators to decide the law correctly or could a conflict of laws analysis prevent this outcome?

More importantly, how will the case of Hall Street Assoc. v. Mattel, Inc., 128 S. Ct. 1396 (2008) affect the situation, at least if a dispute about the validity of an arbitration award is heard in a federal court? (Although the U.S. Supreme Court has held that Sections 2 and 3 of the Federal Arbitration Act apply in state courts, it has expressly refrained from deciding that Sections 9-11 do also). The parties to Hall Street included a provision in their arbitration agreement that any award could be reviewed for error of law. The Supreme Court held that vacatur under the expedited process established in Section 9 of the Federal Arbitration Act was limited to the grounds specified in Section 10. Section 10 provides for vacatur essentially

on the same grounds as Code of Civil Procedure Section 1286.2. Although these, as the court noted in Hall Street, do not include review for error of law, they do provide that an arbitration award shall be vacated if the arbitrators exceed their powers.

The hugely significant question that remains in the wake of Hall Street is whether, when and if faced with a clause identical to that in Cable Connection, the U.S. Supreme Court will find some way to deny review or whether it will distinguish Hall Street and reach the same conclusion the California Supreme Court did. The more immediate practical question is how the various Circuit Courts of Appeal will react.

DEVELOPMENTS IN MEDIATION

In Simmons v. Ghaderi, 44 Cal. 4th 570 (2008), in which the California Supreme Court ruled for the third time (Foxgate was no.1 and Rojas was no. 2) that mediation confidentiality means mediation confidentiality. The defendant physician in a medical malpractice case had granted her carrier authority in writing to agree to any settlement up to $125,000. Based on this authority, the adjuster agreed orally in a mediation to a $125,000 settlement. Before signing the settlement agreement, the adjuster told the physician, who was present at the mediation with her lawyer, but had been excluded from the negotiations, what he had done. At this point, the physician contacted the carrier's general counsel to revoke the authority, and he agreed to the revocation. Thus, neither the adjuster northe physician signed the settlement agreement. A 2-1 majority of the Court of Appeal affirmed a judgment based on the settlement having been agreed to. The majority stated that the defendant's stipulation to events occurring during the mediation "estopped" her to deny the oral settlement. The Supreme Court reversed, holding unanimously that no evidence of what transpired during the mediation conference, including the purported settlement, was admissible. The Court concluded there was no room in Evidence Code Section 1122 for an implied waiver of mediation confidentiality. Among other matters, the Court noted that Sections 1115, et seq. were not in the Privileges segment of the Evidence Code and subject to implied waiver, but were instead part of the segment excluding evidence pursuant to public policy.

Lest we become paranoid about mediation confidentiality, however, we should not forget Evidence Code Section 1121, which provides that otherwise admissible evidence, such as responses to interrogatories, does not become inadmissible when used in mediation.